STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

SUPPLEMENTAL RECOMMENDED DECISION
ON PRICING OF DUCTS AND CONDUITS BY
ADMINISTRATIVE LAW JUDGE JOEL A. LINSIDER

CASE 98-C-1357 - Proceeding on Motion of the Commission to Examine New York Telephone Company's Rates for Unbundled Network Elements.

NOTICE OF SCHEDULE FOR FILING EXCEPTIONS

(Issued June 18, 2001)

Attached is the Supplemental Recommended Decision on Pricing of Ducts and Conduits of Administrative Law Judge Joel A. Linsider in Module 3 of this proceeding, together with a copy of the Commission's rules governing the procedures to be followed. Briefs on exceptions will be due in hand to the undersigned and all active parties on July 9, 2001 and briefs opposing exceptions will be due in hand to the undersigned and may be mailed to all active parties on July 24, 2001.

(SIGNED) JANET HAND DEIXLER
Secretary

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

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APPEARANCES: See Appendix A to Recommended Decision Issued May 16, 2001

JOEL A. LINSIDER, Administrative Law Judge:

INTRODUCTION

As anticipated in my recommended decision issued May 16, 2001, this supplemental recommended decision considers issues raised in Module 3 of this proceeding related to duct and conduit rentals. The procedural history of the case is set forth in the May 16 recommended decision, as are pertinent definitions of terms and identification of parties; the additional item that needs to be noted here is CTTANY's motion, dated March 22, 2001, to strike a portion of Verizon's reply brief or, in the alternative, to accept CTTANY's response to it.

CTTANY's motion challenges the procedural propriety of what CTTANY characterizes as Verizon's argument, in its reply brief, that the calculation method used by CTTANY witness Kravtin "is inconsistent with a specific algebraic approach" said to have been offered for the first time at footnote 309 of Verizon's reply brief "and surrounding pages 116-120."[1] Arguing that Verizon has misused its reply brief to introduce new material, CTTANY urges that the new material be stricken or, in the alternative, that CTTANY be allowed to submit a response to Verizon's allegedly new argument, as set forth in an attachment to the motion.

[1] CTTANY's Motion, p. 2

Verizon responded to CTTANY's motion on March 28, 2001, denying that it improperly used its reply brief and maintaining that it simply offered a more detailed discussion of the issue in a proper response to material in CTTANY's own initial brief. It therefore urges that CTTANY's motion be denied.

As a practical matter, Verizon's answer to the motion also sets forth a detailed substantive rejoinder to the response that CTTANY would have me entertain as an alternative to granting its motion to strike. Having reviewed all of the material submitted by both parties, I believe Verizon's reply brief is procedurally unobjectionable in its scope but that the additional argument offered by both sides provides useful clarification of the issue. CTTANY's motion to strike accordingly is denied; its alternative request to submit the attachment to its motion is granted; and the substantive arguments made by Verizon in its reply to the motion will be taken into account as well.

Conduit rentals differ from nearly all of the other products considered in Module 3 of this proceeding in that they are not classified as unbundled network elements pursuant to the Telecommunications Act of 1996 (the 1996 Act) and are not required by federal law to be priced in accordance with TELRIC. Indeed, the FCC method for pricing conduit (which is not binding on the states) is based on historical costs, and CTTANY urges its use. Verizon, in contrast, urges that conduit rentals, like UNE rates, be set on a forward-looking TELRIC basis, a proposal that would increase the rates very substantially from their present levels, set in 1970 on the basis of historical costs. In addition to these general disagreements, the parties dispute the manner in which their respective methods would be applied.

Before turning to the parties' arguments, it is important to set forth in greater detail the state and federal regulatory context for this issue.

BACKGROUND AND LEGAL CONTEXT

Section 224(a)(4) of the Communications Act of 1934 as amended (47 U.S.C. §224(a)(4)) defines a "pole attachment" as "any attachment by a cable television system or provider of telecommunications service to a pole, duct, conduit, or right-of-way owned or controlled by a utility"; a "utility" is defined in paragraph 1 of that subdivision to include, among other things, "a local exchange carrier" such as Verizon. Section 224 goes on to grant the FCC authority over pole attachment rates, terms, and conditions except where such matters are regulated by a state in accordance with certain conditions specified in the statute.[2] In exercising its authority, the FCC has several times determined that rates for pole attachments, ducts, and conduits should be set on the basis of the utility's historical costs.[3] The FCC's Reconsideration Order also reaffirmed several specific elements of the FCC's costing method that are at issue in this proceeding.

As noted, the statute creates the following exemption from FCC jurisdiction:

> Nothing in [47 U.S.C. §224] shall be construed to apply to, or to give the Commission jurisdiction with respect to rates, terms, and conditions or access to poles, ducts, conduits and rights-of-way as provided in subsection (f), for pole attachments in any case where such matters are regulated by a State.[4]

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[2] 47 U.S.C. §224(b), (c).

[3] See Implementation of §703(e) of the Telecommunications Act of 1996, CS Docket No. 97-151, Report and Order (rel. February 6, 1998)(the Telecom Order); Amendment of Rules and Policies Governing Pole Attachments, CS Docket No. 97-98, Report and Order (rel. April 3, 2000)(The Fee Order); and, most recently, Amendment of Rules and Policies Governing Pole Attachments and Implementation of §703(e) of the Telecommunications Act of 1996, CS Dockets No. 97-98 and 97-151, Consolidated Partial Order on Reconsideration (rel. May 25, 2001)(the Reconsideration Order). The Reconsideration Order was brought to my attention, without comment, in an e-mail sent by counsel for CTTANY on May 29, 2001, with a copy to counsel for Verizon.

[4] 47 U.S.C. §224(c)(1).

Each state that regulates pole attachments is required to certify to the FCC that it does so and that

> in so regulating such rates, terms, and conditions, the state has the authority to consider and does consider the interests of the subscribers of the services offered via such attachments, as well as the interests of the consumers of the utility services.[5]

New York State has asserted jurisdiction over pole attachments through both legislative and regulatory actions.

Section 119-a of the Public Service Law, enacted in 1978, provides as follows:

> The commission shall prescribe just and reasonable rates, terms and conditions for attachments to utility poles and the use of utility ducts, trenches and conduits. A just and reasonable rate shall assure the utility of the recovery of not less that the additional cost of providing a pole attachment or of using a trench, duct or conduit nor more than the actual operating expenses and return on capital of the utility attributed to that portion of the pole, duct, trench, or conduit used. With respect to cable television attachments and use, such portion shall be the percentage of total usable space on a pole or the total capacity of the duct or conduit that is occupied by the facilities of the user. Usable space shall be the space on a utility pole above the minimum grade level which can be used for the attachment of wires and cables.

With specific reference to pole attachments, the Commission determined, in 1997, that New York should exercise its authority over pole attachments by adopting the FCC's approach to pole attachment rates, which called for the use of historical costs rather than the forward-looking incremental costs pertinent to the pricing of unbundled network elements.[6] In so doing, the Commission said:

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[5] 47 U.S.C. §224(c)(2)(B).

[6] Case 95-C-0341, Pole Attachment Issues, Opinion No. 97-10 (issued June 17, 1997).

> Since the enactment of the Telecommunications Act of 1996 there has emerged a clear need for cooperative federalism in this and other areas of telecommunications so as to provide consumers the full benefits available from the development of competitive markets.
>
> By embarking on this course, we hope to make it easier for service providers to do business by eliminating unnecessary variation in regulatory requirements. Also, by exercising our authority in this manner, we make it possible for firms operating nationally to compare favorably New York's practices and those followed elsewhere. Of course, we shall retain our primary jurisdiction over pole attachments and continue to evaluate such matters. If ever there were reason to depart from the federal approach, in order to protect the public interest, we would consider such action.[7]

Verizon later argued, in connection with the proposed inclusion of duct and conduit pricing in Phase 3 of the First Network Elements Proceeding, that the Commission's adoption of the FCC's historical-cost method for pole attachments applied to ducts and conduits as well.[8] As noted, Verizon now urges rejection of the FCC's method and adoption, instead, of forward-looking pricing; it acknowledges the change in its position since 1998, explaining that its "current views have emerged from the comprehensive review and re-evaluation of costing and pricing issues that we undertook in this proceeding."[9]

Finally, it should be noted that ducts and conduits in Manhattan and the Bronx are owned not by Verizon but by its wholly owned subsidiary, Empire City Subway, Limited. Empire City Subway, which offers conduit space to Verizon and other

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[7] Id., p. 6.

[8] Cases 95-C-0657 et al., First Network Elements Proceeding, Ruling on Consideration in Phase 3 of Ducts, Conduits, and Rights-of-Way (issued March 9, 1998), citing Verizon's (then New York Telephone's) March 3, 1998 Motion for Clarification, p. 2.

[9] Verizon's Initial Brief, p. 219, n. 501.

carriers on a nondiscriminatory basis, is regulated not by the Commission but by the New York City Department of Information Technology and Telecommunications.

OVERVIEW OF PARTIES' POSITIONS AND COSTING METHODS

Verizon

Verizon asserts that its current rate of 75¢ per foot per year is grossly understated inasmuch as it was set in 1970 on the basis of even earlier costs and has not been changed since; it notes that the rate is far below the corresponding rates in other states within its footprint.

Verizon proposed a forward-looking costing method that takes account of the current cost of construction for new conduit systems. Along with the investment, it allocates known tax and maintenance costs among conduit users to derive an annual rental cost per foot and apportions unusable or spare space through application of a utilization factor.[10] To determine conduit construction costs, Verizon used current contract prices applied to a hypothetical construction project. It deaveraged costs into values representing the major cities and rest-of-state zones; that process did not include Manhattan and the Bronx, where conduit is provided by Empire City Subway.

The rates resulting from Verizon's study (and the current rates for comparison purposes) are as follows:

	Conduit Rates (per duct-foot)		
	Current Rate	Proposed	
Proposed	(Statewide)	Major Cities	Rest-of-State
Main Conduit[11]	$0.75	$6.22	$5.41
Subsidiary Conduit	$1.40	$9.49	$7.68

[10] Verizon's Initial Brief, pp. 222-223, citing Tr. 2,497-2,512.

[11] Main conduit and subsidiary conduit are defined below.

In its rebuttal testimony, Verizon offers three alternative methods in the event the Commission declines to adopt its primary, TELRIC-based proposal. Two of the alternatives involve modifications to the FCC's formula; the third would simply apply an inflation factor (the change in the Telephone Plant Index) to the rates set in 1970. That method results in a main duct rental of $3.03 per for per year and a subsidiary duct rental of $5.65 per foot per year.[12]

Verizon objects to CTTANY's suggestion, discussed below, that the Commission assert jurisdiction over Empire City Subway's rates.

CTTANY

CTTANY offers an analysis based on the FCC's historical cost method. It begins with embedded costs reported in publicly available ARMIS data, from which it calculates a net (of accumulated depreciation and accumulated deferred taxes) conduit investment figure. It divides that net figure by the total system conduit length to arrive at the net linear cost of conduit, and it multiplies that cost by a carrying charge factor to translate investment costs into annual costs. It multiplies that result by a measure of the percentage of conduit capacity occupied by an attacher in order to calculate the maximum rate.

In calculating net linear cost, CTTANY proposed to use not ARMIS data, which it regarded as unreliable, but information available from Verizon's continuing property records (CPR). On the basis of that analysis, CTTANY calculated a maximum rate per foot of 80¢.

Characterizing the Empire City Subway situation as an "historical accident,"[13] CTTANY urges the Commission to recognize Verizon's control over Empire City Subway and assert jurisdiction over the subsidiary.

[12] Tr. 3,446.

[13] CTTANY's Initial Brief, p. 45.

HISTORICAL VERSUS FORWARD-LOOKING COSTING

As already noted, CTTANY urges that ducts and conduits continue to be priced on the basis of historical costs, consistent with the FCC's method and, in its view, as required by New York Law. Verizon, maintaining that forward-looking costing is superior for a wide range of policy reasons, offers a different reading of the New York statute, stresses the federal deference to states that have undertaken to regulate duct and conduit pricing on their own, and disputes the reasoning underlying the FCC's continued endorsement of historical cost pricing. For the reasons described below, I recommend that the Commission continue to price conduits and ducts on the basis of historical costs.

Arguments

1. Verizon

Its general objections to TELRIC notwithstanding, Verizon believes that if the standard is used for the pricing of UNEs, it should be applied to conduit as well for the sake of fairness--use of TELRIC should not be limited to situations where it produces lower costs--and of economic logic and methodological consistency, to ensure economically efficient decisions between leased conduit and full unbundled loops (which are to an extent economic substitutes for each other). Noting that the FCC's decisions on conduit pricing are not binding on the Commission, Verizon nevertheless goes on to dispute the reasons cited by the FCC in support of its decision to price conduit on the basis of historical costs:

- The FCC cited stability and simplicity in support of maintaining the status quo; Verizon sees no reason to exempt conduit from the rate changes contemplated in this proceeding and sees no reason for simplicity to be a decisive consideration.
- The FCC noted the complicated procedures that would be needed to develop a new, forward-looking ratemaking formula; Verizon points out that this proceeding has already done so.

- The FCC held that the advantages of forward-looking pricing were likely to be less pronounced in the pole attachment context; Verizon regards that contention as baseless, arguing that even though conduit facilities are not built or replaced on a unit-by-unit, as needed basis, new conduit does need to be built as demand expands.

- The FCC noted the absence of any congressional directive to deviate from the use of historical costs; Verizon reiterates its point that the FCC's regulations are not binding here.

- The FCC noted that its notice has not specifically raised the possibility of moving to forward-looking costing; Verizon notes that this procedural objection likewise is inapplicable here.

With respect to state law, Verizon argues that the final two sentences of PSL §119-a (set forth above), which suggest reference to historical costs, apply only to "cable television attachments and use" and have no bearing on the pricing of conduit made available for telecommunications purposes, the subject of the present inquiry. In its view, the pertinent wording is the second sentence, defining a "just and reasonable rate," and it contends that the reference there to "actual" costs does not limit recovery to historical costs: "historical costs are costs that Verizon has incurred in the past; forward-looking costs are costs that it incurs in the present and will incur in the future to replace or augment its network, and both are 'actual' if they are correctly computed."[14] Verizon recognizes the Commission's determination, in Opinion No. 97-10, to adhere to the FCC pricing formula for poles in the interest of "cooperative federalism," but it contends that the UNE rates set in this proceeding will differ from those set in other states and that there is more need for consistency between UNE pricing and conduit pricing than there is to conform state rates to a federal model.

[14] Verizon's Initial Brief, p. 220 (footnote omitted).

Verizon disputes the relevance of CTTANY's emphasis, described below, on the bottleneck nature of conduit; it contends that its own method would apply to conduit pricing the regime that the FCC has mandated for network elements that meet the statutory requirements for unbundling. Verizon adds that CTTANY's members should not be charged a sub-compensatory rate "simply as a reward for purchasing a supposed monopoly product."[15] It likewise disputes CTTANY's argument, also discussed below, that historical costs should be relied on because conduit facilities are well below exhaust level and a request for conduit will not necessarily trigger a need to deploy new facilities. It argues that this is just as true for loops and that the existence of spare capacity "is essentially irrelevant to TELRIC analysis," which assumes proper allocation over the entire demand of the entire element level of forward-looking investment. Verizon suggests, therefore, that CTTANY is criticizing TELRIC more than drawing a distinction between conduits and loops.[16] Verizon notes as well that any claim that the existence of spare capacity means that conduit has an incremental cost of zero would be based on short-run incremental cost, which no party advocates as a basis for prices.[17]

2. CTTANY

CTTANY argues generally that conduits are an essential bottleneck facility and that incumbent local exchange carriers "have long sought to maximize their leverage control over pole and conduit resources to protect their stranglehold in their core voice telephony business, and to facilitate their entry into the cable television and broadband communications markets."[18] CTTANY contends that federal and state regulation of poles and conduit was designed to ensure access to those facilities, and it

[15] Verizon's Reply Brief, p. 114.

[16] Id., pp. 114-115.

[17] Verizon's Initial Brief, pp. 221-222.

[18] CTTANY's Initial Brief, p. 3.

disputes what it characterizes as Verizon's suggestion that cable operators are no longer fledgling businesses requiring that regulatory protection.

CTTANY presents a detailed account of the history of historical cost pricing under federal law, going back to the enactment of 47 U.S.C. §224 in 1978 and continuing through the FCC's adoption of the Fee Order in April 2000.[19] It contends as well that PSL §119-a calls for pricing on the basis of historical costs, charging that Verizon asks the Commission to disregard that statute and asserting that the statute does not distinguish between cable operators that provide video services and those providing dialtone as well. It cites an FCC determination that the term "cable system" is not limited to a facility that provides only cable service and includes those providing other communication services as well and contends that "accordingly, at a minimum Section 119-a governs rates for telecommunications services provided by cable operators over cable systems, and cannot be ignored in this proceeding."[20] (As noted, Verizon in its response stresses that the sentence of §119-a at issue begins "with respect to cable television attachments and use." It argues that it therefore does not apply to telecommunications services and that there is no basis for asserting that a CLEC that happens to be a cable television provider should be entitled to a lower rate than a CLEC that is not.[21])

CTTANY goes on to cite the Commission's support of historical cost pricing in Opinion No. 97-10, stressing the Commission's recognition of the need for "cooperative federalism"[22] and asserting that its reasoning applies to conduit rental just as much as to pole attachments. It suggests that

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[19] As noted above, in an action taken after briefing in this proceeding was completed, the FCC in the Reconsideration Order reaffirmed the use of historical costs.

[20] CTTANY's Initial Brief, p. 14.

[21] Verizon's Reply Brief, p. 121.

[22] CTTANY's Initial Brief, p. 15, citing Opinion No. 97-10, p. 6.

Verizon's earlier endorsement of the FCC formula may be attributed to the pendancy of its §271 application, and that its change of position, and its efforts now to seek much higher rates on the basis of forward-looking costs, result from the application having been granted. Finally, CTTANY asserts that adoption of the FCC method for costing pole attachments and conduits is consistent with the market-opening purposes of the 1996 Act.[23]

CTTANY contends as well that forward-looking pricing--which it refers to as "reproduction cost pricing"--should not be applied to conduit inasmuch as it is constructed solely for Verizon's needs, generates no additional capital cost when it is rented out to third parties, and constitutes a long-lived asset unlikely to be reproduced. Verizon is not obligated to install new conduits to meet new demand, and it recovers the cost associated with modifying conduit to accommodate additional facilities--termed "make ready" costs--through a separate charge. It notes that Verizon's existing conduit is nowhere near exhaust, that main conduit has an average service life of 80 years, and that conduit requires no ongoing reinvestment in innovative technologies. CTTANY adds that the use by third parties of Verizon conduit in fact increases Verizon's conduit capacity inasmuch as Verizon typically requires cable operators to pull "inner duct"--that is, small pipes or tubes placed inside a conventional duct to allow the installation of multiple wires or cables--in order to create additional pathways within a conduit that is made available. CTTANY characterizes this requirement as "akin to a forced capital contribution by the renter that increases the capacity and useful life of Verizon's plant. . . . Verizon retains title to the inner duct and may use or lease the duct space that is not used by the cable operator."[24] (Verizon characterizes the argument that capacity is increased as "contrary to common sense, not to mention the laws of physics,"

[23] CTTANY's Initial Brief, p. 17.

[24] Id., p. 11.

and asserts that by pulling inner duct, a CLEC merely preempts use of a smaller portion of the total conduit than it otherwise would, but does not increase the space that was available to Verizon before the CLEC's occupancy.[25])

CTTANY disputes Verizon's claim that conduit should be priced on the same basis as network elements in order to promote economically efficient choices between the two modalities. It contends that cable operators--"the single most promising source of facilities-based competition in New York"[26]--are already in the conduit and will not abandon facilities-based service in favor of UNE leasing. Citing the reasons offered by the FCC for reaffirming its method, CTTANY emphasizes the predictability and reliability of the method and again sees no basis for distinguishing conduit from poles. It charges that Verizon "flatly ignores the substantial body of federal and state laws that recognize and regulate both poles and conduits as essential facilities critical to the success of facilities-based competition," asserts that "the overwhelming majority" of states have joined the FCC in rejecting forward-looking pricing here, and cites Ameritech's proposal to use the FCC method in an Illinois Commerce Commission proceeding.[27] Finally, CTTANY emphasizes the Commission's endorsement of the FCC method in Opinion No. 97-10, Verizon's strong endorsement of the FCC method in the First Network Elements Proceeding, and Staff's rejection over the years of Verizon's (then New York Telephone's) earlier interest, preceding its position in the First Element Proceeding, in pricing pole attachments and conduit usage on a forward-looking basis.[28]

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[25] Verizon's Reply Brief, p. 114, n. 299.

[26] CTTANY's Reply Brief, p. 4.

[27] Id., pp. 6-7.

[28] CTTANY recognizes that the Commission never formally rejected a forward-looking method for pricing conduits, noting that New York Telephone withdrew its proposals each time it met with resistance from Staff. Verizon, for its part, discounts the importance of this history, characterizing as irrelevant

Discussion

Verizon is correct in arguing that the Commission is not bound by the FCC's decisions with regard to conduit pricing and that PSL §119-a need not be read to require basing prices on historical costs.[29] But it is far less persuasive in arguing that the Commission should use its discretion here to depart from the FCC's pricing method.[30]

Essentially, Verizon insists on the need for consistency between the pricing of conduit rentals on the one hand and of UNEs on the other. But the FCC, the author of TELRIC pricing for UNEs, appears to see no need for that consistency, having very recently reaffirmed historical-cost-based pricing of poles and conduits; and this Commission, as a matter of discretion, has deferred to the FCC in this regard, at least with respect to pole attachments. I see no reason why conduits, whose function is analogous so that of poles, should be treated any differently from them, and the Commission's decision in Opinion No. 97-10 seems controlling here. That, indeed, was Verizon's own position in the First Elements Proceeding, and its attribution of its changed position only to its "comprehensive review and re-evaluation of costing and pricing issues" inevitably suggests a degree of result orientation.

Staff's attitude on this issue in the 1980s and early 1990s and urging that the matter be decided in light of the law and facts here set forth. Verizon's procedural point is well taken.

[29] That said, it seems odd for Verizon to argue that the reference in §119-a to actual costs does not preclude TELRIC pricing when it has argued elsewhere that TELRIC is flawed by its failure to allow recovery of actual costs.

[30] References in this section to "the FCC's method" are to the use, in general, of historical costs. How that method should be applied, and whether CTTANY has done so properly, are taken up in the next section.

Beyond that, it does not appear that forward-looking duct and conduit technology differs all that much from historical. In contrast to the UNE situation, this is not a case where TELRIC pricing is needed to avoid imposing on CLECs the costs associated with the incumbent's embedded plant (and embedded inefficiencies). Verizon's plea for consistency between UNE pricing and duct and conduit pricing fails to take account of the differences between the two products.

Accordingly, I see no basis for recommending what would be, in effect, a reversal of Commission precedent. Consistent with the Commission's earlier determination with respect to pole attachments, rates for duct and conduit rentals should be set, following the FCC's method, on the basis of historical costs.

In view of that recommendation, there is no need to consider here CTTANY's specific critique of Verizon's costing method. But before turning to Verizon's specific critique of CTTANY's application of the FCC method, it is necessary to take up Verizon's alternative proposals.

VERIZON'S ALTERNATIVE PROPOSALS

Verizon offered three pricing proposals for the Commission's consideration in the event the Commission wished to consider alternatives to the FCC's approach that stopped short of moving to fully TELRIC-based pricing. The first two proposals would modify the FCC's method to incorporate alternative ways of reflecting the asserted costs of usable and unusable space. Verizon and CTTANY dispute the details of both methods and Verizon successfully refutes some of CTTANY's specific criticisms.[31] But Verizon ultimately misstates the issue when it says "what CTTANY fails to demonstrate is that Verizon's approaches are in any way inferior to the FCC

[31] CTTANY's Initial Brief, pp. 37-42; Verizon's Reply Brief, pp. 124-126.

methodology."[32] Much more significantly, Verizon has failed to demonstrate that its methods are in any way superior to the FCC method, which the Commission has already determined should be adopted for pole attachments, or that its proposed modifications correct any flaws in that method other than its production of a rate that Verizon deems too low.

Verizon's third alternative would apply to the existing rate, as set in 1970, an inflation factor equal to the change in the Telephone Plant Index (TPI) for the conduit account since 1970. CTTANY argues that the acceptance of this method requires granting that the rate was correctly developed in 1970, something no longer possible to verify, and it suggests that the 1970 rates might well have been inflated in view of Verizon's monopoly control over pole and conduit plant. Notwithstanding the supposed simplicity of the method, CTTANY sees no reason to hypothesize investment using an inflation adjuster when the real data are readily available in ARMIS.

Verizon responds that the 1970 rate was based on a cost study submitted by New York Telephone and approved by the Commission and that there is no reason to assume that that review would have accepted an inflated rate. It contends as well that the real data available in ARMIS comprise data on booked, depreciated investment rather than on the current cost of constructing conduit.

[32] Verizon's Reply Brief, p. 124.

Applying an inflation factor to a 30-year-old rate might be warranted as a stop-gap measure if it were impossible, for some reason, to directly calculate a rate now. That is not the case, and the record provides ample basis for a new rate determination. And even if an inflation factor were to be applied, it would not be the unadjusted TPI; it would be necessary to recognize, among other things, an offset for productivity improvement.

Accordingly, I recommend that Verizon's alternative methods be rejected and that rates be set on the basis of the FCC method, the details of which are next addressed.

APPLICATION OF THE FCC METHOD

Cable Television Attachments v. Telecommunications Attachments

As a threshold matter, Verizon suggests that CTTANY improperly used the FCC formula applicable to cable television attachments rather than the method applicable to telecommunications providers, which produces a higher rate. CTTANY responds that the theoretical difference between the two methods is the inclusion, in the telecommunications formula, of a component related to unusable space and that the FCC has now clarified that there is no unusable space, effectively making the two methods equivalent.[33]

CTTANY is correct; in its most recent pronouncement on the matter, the FCC said that "essentially the lack of any unusable capacity in a conduit makes the practical application of the Pole Attachment Act formulas the same for both cable attachers and telecommunications attachers both before and after February 8, 2001."[34]

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[33] Verizon's Initial Brief, p. 228; CTTANY's Reply Brief, pp. 11-12.

[34] Reconsideration Order, ¶88 (footnotes omitted).

Use of CPR Data Rather Than ARMIS

The principal dispute between the parties over CTTANY's application of the FCC formula relates to CTTANY's resort to CPR data, rather than ARMIS data, to determine the number of duct-feet over which net conduit investment should be spread, and to the manner in which it used those CPR data. Before considering this issue, reference must be made to some pertinent definitions:

> Conduits are structures that provide physical protection for cables and allow new cables to be added inexpensively along the pathway or route. A conduit consists of one or more ducts, which are the enclosures that carry the cables. Often, when a cable operator's or telecommunication carrier's cables are placed in a duct, three or more inner duct are inserted into the duct allowing "one duct to be treated more like conduit."[35]
>
> "Duct" feet refers to the total length of conduit ductwork in the network. "Trench" feet refers to the total length of the trenches in which the conduit is buried. The relationship between conduit feet and duct feet depends on the average number of ducts buried in each trench.[36]

In other words, the number of duct-feet will be equal to or greater than the number of trench-feet, depending on whether the number of ducts in the conduit is one or greater than one.

Finally, "main conduit" refers to a bank of conduit that directly connects two manholes or a central office vault and a manhole, along with certain associated equipment. Subsidiary conduit refers to conduit extending from manholes to poles or buildings (other than central office buildings) that is required to extend underground cables to connections with either aerial or block cables.

On the basis of its ARMIS data, Verizon calculated a total of 265.5 million duct-feet. That figure, together with net

[35] Reconsideration Order, ¶87.

[36] Verizon's Reply Brief, p. 116, n. 303. Verizon adds that "CTTANY's brief refers to trench feet as 'conduit' feet."

conduit investment of about $903 million,[37] produces a net investment per duct-foot of about $3.40.

CTTANY, however, regarded Verizon's duct-to-conduit ratio of 3.8, based on ARMIS data, as out of line with the ARMIS-based duct-to-conduit average ratio of 5.74 in the remainder of the former Bell Atlantic footprint. It therefore turned to Verizon's continuing property records, a detailed physical inventory system that it regarded as likely to be more accurate than ARMIS, noting that the FCC approach generally relied on publicly available reports such as ARMIS but permitted use of more accurate data when available. Verizon's CPR data showed the average number of ducts per main conduit to be 7.91. CTTANY's witness Kravtin reduced that figure to 7.21 ducts per conduit to reflect the lower number of ducts to be found in subsidiary conduit. The adjustment was based on Verizon's evidence that there were two ducts in subsidiary conduit, a figure that witness Kravtin then weighted on the basis of the ratio of main to subsidiary duct derived from Verizon's CPR.[38]

Verizon objects both to CTTANY's reference to the CPR data and to the manner in which it used those data. It notes that the CPR data as used by CTTANY produce a duct-foot to trench-foot ratio that is about as far above the Bell Atlantic footprint average as the ratio based on ARMIS data is below it; that a lower average level of ducts per trench in New York than in other parts of the footprint may be attributable to local conditions, such as the considerable amount of relatively small cross-section conduit systems in suburban areas[39]; and that, in any event, there is no discrepancy between the CPR data and the ARMIS data if the CPR data are correctly used to simply determine the total duct-footage over which the investment should be spread.

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[37] Gross investment of $1.336 billion, reduced for depreciation and deferred taxes. (Verizon's Reply Brief, p. 116.)

[38] CTTANY's Initial Brief, pp. 21-24 and record citations there referenced.

[39] Verizon's reply to CTTANY's motion to strike, p. 5, n. 11.

The discrepancy arises, Verizon continues, because of what it sees as CTTANY's misapplication of the CPR data to produce a weighted average of 7.21 duct-feet to conduit-feet. That figure, it maintains, is based on weighting the number of duct-feet of main and of subsidiary conduit, which overstates the effect of the mainline conduit, which has a substantially greater number of ducts per conduit. That calculation thereby increases the weighted average and reduces the investment per duct-foot. Verizon suggests that the correct way to compute the weighted average would be to do so on the basis of the number of mainline and subsidiary trench-feet, a calculation that would produce a result equal to the result produced by simply dividing net investment by total duct-feet.[40] In its reply to CTTANY's motion to strike, Verizon presents a numerical example showing that CTTANY's weighting method produces a cost per duct-foot that, when multiplied by the total number of duct-feet, yields a cost figure well below the figure initially posited.[41]

Verizon objects further that trenching entails substantial fixed costs that do not vary with the number of ducts and that subsidiary conduit systems with smaller number of ducts per trench therefore have a significantly higher cost per duct than mainline systems. The average cost per duct therefore is understated by CTTANY's understatement of the contribution made by subsidiary ducts.[42]

In response, CTTANY maintains that Verizon has failed to explain the discrepancy between its New York duct-to-conduit

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[40] It is this calculation, set forth in alegebraic terms at p. 119, n. 309 of Verizon's reply brief, that is central to CTTANY's motion to strike. As noted above, I am denying the motion to strike and entertaining both CTTANY's further reply appended to its motion and Verizon's surreply incorporated in its response to the motion. Verizon's reply brief was in no way improper, but each of the ensuing pleadings further clarifies the issue.

[41] Verizon's response to CTTANY's motion, p. 7, n. 14.

[42] Verizon's Reply Brief, p. 120.

ratio and those in other parts of its footprint. It disputes Verizon's charge that it has overstated the contribution of mainline conduit, noting that its ratio of main to subsidiary conduit is derived from Verizon's own CPR data and that Verizon has not offered an alternative weighting. It suggests that Verizon is abandoning the ratio in its CPR "because of the results produced by its application in the FCC formula,"[43] and it notes that its members rent almost exclusively mainline conduit and that the rate would have been even less than its witness calculated had the number of ducts per mainline conduit been used.

Verizon's challenge to CTTANY's adjustment is persuasive. In effect, CTTANY is double-counting the greater number of ducts in main conduit: once to determine the weighting to be afforded main conduit and once to determine the number of ducts to which the weighting is to be applied. The proper weighting would be on the basis of main and subsidiary trench- feet, and that weighting would then be applied to the larger number of ducts in main conduit, thereby recognizing that larger number only once. As Verizon has shown, that correct weighting produces, as would be expected, a cost per duct-foot identical to the one produced by simply dividing net investment by the number of duct-feet. Accordingly, I recommend that the rate be set on the basis of the FCC method, using a cost per duct-foot calculated by dividing net investment by the number of duct-feet shown in the ARMIS data, and without reference to the CPR data.

Half-Duct Presumption

To facilitate calculation of a rate reflecting the percentage of conduit capacity occupied by an attachment, the FCC adopted in the Fee Order and the Telecom Order, and reaffirmed in the Reconsideration Order, a rebuttable presumption that the

[43] CTTANY's supplement to its reply brief, as attached to its motion to strike, unnumbered second page.

attacher occupies one half of a duct.[44] In other words, unless the presumption is rebutted, the attacher is charged a rate based on one-half of the calculated cost per duct-foot. The FCC added that "when the actual percentage of capacity occupied is known, it can and should be used instead of the one half duct presumption," and that "the presence of inner duct is adequate rebuttal. Where inner duct is installed, either by the attacher or in a previous installation, the maximum rate will be reduced in proportion to the fraction of the duct occupied. That fraction will be one divided by the actual number of inner ducts in the duct."[45]

In light of those provisions, CTTANY presented rates for a full duct, a half duct, one-third of a duct, and one-quarter of a duct, to be applied depending on the number of inner ducts installed. Verizon objected, contending that the half-duct premise should be applied inasmuch as "Verizon would not, except in extraordinary circumstances, occupy the same duct as a CLEC."[46] In its own study, Verizon calculated rates for a whole duct and a half duct only. CTTANY contends, however, that where inner duct is used, the attacher typically occupies less than half of the duct and that the FCC's process for rebutting the half-duct presumption recognizes that reality.

Although Verizon contends that CTTANY ignores Verizon's testimony that it would not typically occupy the same duct as a CLEC, that testimony does not really undermine the basis for the FCC's conclusion that the presence of inner ducts rebuts the half-duct presumption. Verizon's witness went on to acknowledge on cross-examination that it retains custody of the inner ducts not used by the attacher along with the option to lease that capacity out to another attacher.[47] There is, accordingly, no reason to question the FCC's premise that the

[44] Reconsideration Order, ¶¶95-98 and history there cited.

[45] Reconsideration Order, ¶98.

[46] Verizon's Reply Brief, p. 120, citing Tr. 5,756-5,757.

[47] Tr. 5,757.

presence of inner duct rebuts the presumption and warrants assigning the attacher a correspondingly lower proportion of the total cost. I recommend, accordingly, adoption of CTTANY's proposal to set the rate on the basis of the number of inner ducts present.

ACCESS TO RIGHTS-OF-WAY

Verizon proposed to continue charging on an individual case basis (ICB) for access to private rights-of-way that it owns or controls. In effect, it would flow through, on a prorated basis, the fee that it itself pays; that fee will vary widely, given the diverse nature of the real property interests involved.

CTTANY notes that most right-of-way expenses are incorporated into the conduit rent itself, and it infers from cross-examination of Verizon's witness Brant that Verizon "only intends to use ICB pricing in the most unusual circumstances where Verizon is not in the public right of way but instead is on private property and the costs have not been internalized into the conduit rental."[48] It asks the Commission to clarify that this is the case and to express its willingness to entertain complaints about such pricing if the parties cannot reach agreement.

Verizon responds that its ICB proposal does not apply at all to rights-of-way associated with conduit rental but only to "'naked' rights-of-way, i.e., to rights-of-way that a CLEC seeks to 'sublet' from Verizon for the deployment of its own conduit. . . . It would not apply to the rates for facilities such as loop or conduit that already incorporate relevant right of way costs through the application of [annual cost factors]."[49] Verizon adds that there is no distinction to be drawn in this regard between public and private rights-of-way.

[48] CTTANY's Initial Brief, p. 44.

[49] Verizon's Reply Brief, p. 127 (emphasis in original).

Verizon's clarification of its proposal is adequate; naked rights-of-way, whether public or private, should continue to be priced on an individual case basis.

CONDUIT OWNED BY EMPIRE CITY SUBWAY

As noted at the outset, conduit in Manhattan and the Bronx is owned by Verizon's wholly owned subsidiary, Empire City Subway, an entity regulated by the New York City Department of Information Technology and Telecommunications rather than by the Commission. CTTANY asks the Commission to assume jurisdiction over these rates or to declare that the FCC has plenary jurisdiction over them inasmuch as the City of New York has not certified to the FCC that it has assumed jurisdiction.

CTTANY argues that Verizon owns and controls Empire City Subway. It is irrelevant, in its view, that title to the conduit resides in the subsidiary, inasmuch as an ILEC's obligations with regard to conduit access depend on control rather than on ownership. CTTANY contends as well that as part of its §271 application, Verizon acknowledged that Empire City Subway is governed by the 1996 Act and its market opening obligations and asserts "it would be intolerable to allow Verizon into the long-distance business based on an unbundling representation that it is now breaking."[50]

CTTANY further alleges that Verizon's practices with respect to Empire City Subway rates charged to itself violate the FCC's affiliate transaction rules and that Verizon pays Empire City Subway a rental far less than what it proposes to charge third parties. Acknowledging the 1982 court decision holding that the Commission did not have jurisdiction over Empire City Subway,[51] CTTANY suggests that such "accidental advantages of incumbency" were supposed to be overturned by the

[50] CTTANY's Initial Brief, p. 47.

[51] New York State Cable Television Association v. PSC, 87 A.D. 2nd 288 (3rd Dep't, 1982).

1996 Act. It asserts Verizon is attempting to exempt Empire City Subway form the jurisdiction of the FCC and this Commission on the basis of "the fiction that the companies are separate entities."[52]

In response, Verizon notes the Commission's past disclaimer of jurisdiction over Empire City Subway's rates and the Third Department's holding to the same effect. It suggests that "CTTANY's efforts to persuade the Commission to assume jurisdiction notwithstanding the court's ruling (and its own prior determination) are, quite simply, an invitation to lawlessness" and should be disregarded.[53] Verizon adds that CTTANY's charge with respect to the FCC's affiliate transaction rules is beyond the Commission's jurisdiction and, in any event, is unfounded inasmuch as the transactions may be accounted for at tariffed rates, and Empire City Subway's rates are tariffed with New York City. Similarly, it contends, the FCC's authority over Empire City Subway's rates is beyond this Commission's jurisdiction.

Verizon's arguments on this point are well taken. CTTANY's proposal would have the Commission disregard its own long-standing precedent as well as the determination of the courts and should not be further considered.

SUMMARY OF RECOMMENDATIONS

Rates for ducts and conduits should be set on the basis of the FCC's method without the adjustment proposed by CTTANY. Those rates are calculated in the Appendix.

Rights-of-way should continue to be priced on an individual case basis.

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[52] CTTANY's Initial Brief, p. 48.

[53] Verizon's Reply Brief, p. 128.

The Commission should continue to recognize that the rates of Empire City Subway Limited are not within its jurisdiction.

JAL:gds
June 18, 2001

Verizon New York Inc.
Derivation of Recommended Duct and Conduit Rates per RD

Line #	Item	Source	Amount
1	Gross Conduit Investment	1999 ARMIS	$1,335,713,000
2	Accumulated Depreciation for Conduit	1999 ARMIS	401,098,000
3	Accumulated Deferred Income Taxes for Conduit	1999 ARMIS	31,534,212
4	Net Conduit Investment	(L1-L2-L3)	903,080,788
5	System Duct Length (Feet)	1999 ARMIS	265,472,494
6	Net Conduit Investment per Duct Foot	L4/L5	3.40
7	Carrying Charge Factor	1999 ARMIS	43.97%
8	Maximum Rate Per Full Duct Foot	L6*L7	$1.50
9	Rate Per Half Duct	L8/2	$0.75
10	Rate Per Third Duct	L8/3	$0.50
11	Rate Per Quarter Duct	L8/4	$0.37